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March 12, 2004

VIA ELECTRONIC SUBMISSION

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW – Lobby Level
Washington, D.C. 20554

Re: ***Notice of Ex Parte -- Petition for Declaratory Ruling that AT&T's Phone-to-Phone IP Telephony Services Are Exempt from Access Charges, WC Docket No. 02-361***

Dear Ms. Dortch:

On behalf of SBC Communications, Inc. (SBC), I am writing to respond to a recent *ex parte* filed by AT&T regarding the above-referenced petition.[1] As SBC has already demonstrated at length, AT&T is flagrantly violating the Commission's rules by refusing to pay access charges on plain old long distance service that AT&T chooses to transport over an Internet Protocol (IP) network for some distance between points on the public switched telephone network.[2] Now, amid press reports that the Commission is poised to deny its petition,[3] AT&T is attempting to delay that outcome by offering up dubious legal arguments at the last minute. Most of these arguments have already been discredited by SBC and others. SBC takes this opportunity, however, to briefly address two matters in AT&T's recent filing.

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[1] *Ex Parte* Letter from Pat Merrick, AT&T, to Marlene Dortch, FCC, WC Docket No. 02-361 (Feb. 20, 2004) (AT&T Memorandum).

[2] *See* Opposition of SBC Communications, Inc., WC Docket No. 02-361 (Dec. 18, 2002); Reply Comments of SBC Communications, Inc., WC Docket No. 02-361 (Jan. 24, 2003); *Ex Parte* Letter from Gary Phillips, SBC, to Marlene Dortch, FCC, WC Docket No. 02-361 (Dec. 19, 2003); Memorandum by SBC Communications, Inc., Urging the Commission to Deny AT&T's Access Charge Avoidance Petition, WC Docket Nos. 02-361, 03-211 & 03-266, January 14, 2004 (SBC Memorandum), attached as an exhibit to *Ex Parte* Letter from James Smith, SBC, to Michael Powell, FCC, WC Docket No. 02-361 (Jan. 14, 2004).

[3] *See* Communications Daily, Wireline (Feb. 17, 2004) ("The FCC reportedly is close to voting down AT&T's petition seeking an exemption from access charges for calls transported on its IP backbone.")

First, contrary to AT&T's claims, the Commission's 1998 *Report to Congress* did not announce an "interpretive" rule that can be used to shield AT&T from its obligation to pay retroactively for the past due access charges it has unlawfully avoided.[4] Second, AT&T has mischaracterized the holding of an important Supreme Court decision (*SEC v. Chenery*), which actually provides no support for AT&T's arguments. The fact that AT&T is reduced to these tactics is telling. AT&T's petition has been pending for nearly seventeen months, during which time AT&T has repeatedly attempted to twist the facts and distort the law. But the facts and the law are, and always have been, perfectly clear: AT&T is offering nothing more than standard long distance telephone service for which it is required to pay access charges under well-established Commission rules. The Commission should promptly deny AT&T's petition and put an immediate end to AT&T's unlawful access charge avoidance scheme.

(1) The *Report to Congress* Did Not -- and Legally Could Not -- Announce an Interpretive Rule That Would Shield AT&T from Its Obligation to Retroactively Pay for the Past Due Access Charges It Has Avoided.

SBC has previously explained that, despite AT&T's arguments to the contrary, the *Report to Congress* did not modify the Commission's access charge rules.[5] Indeed, as SBC made clear, the *Report to Congress* could not have lawfully altered section 69.5 of the Commission's access charge rules to exempt AT&T from paying access charges on IP-in-the-middle long distance service because, among other things, the Commission never gave prior notice of any such ostensible rule change, as would have been required under the Administrative Procedure Act (APA).[6] In an attempt to shore up this hole in its argument, AT&T now asserts that the *Report to Congress* announced an "interpretive" rule exempting it from access charges, which is not subject to notice and comment procedures under the APA.[7] According to AT&T, any decision from the Commission requiring it to pay access charges now would therefore qualify as a "new" rule that would displace the "old" rule purportedly announced in the *Report to Congress*.[8] As AT&T points out, under D.C. Circuit precedent, when a new rule replaces an old rule, "a decision to deny retroactive effect is uncontroversial."[9] Thus, under AT&T's theory, the Commission's interpretive rule would shield it from any obligation to pay retroactively for the access charges it has avoided since the issuance of the *Report to Congress*.

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[4] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report to Congress, 13 FCC Rcd 11501 (1998) (*Report to Congress*).

[5] SBC Memorandum at 4-9.

[6] SBC Memorandum at 7-9. The *Report to Congress* also failed to include ordering clauses that accompany rule changes and it was never published in the Federal Register.

[7] AT&T Memorandum at 11-22.

[8] AT&T Memorandum at 14.

[9] *Verizon Telephone Cos. v. FCC*, 269 F.3d 1098, 1109 (D.C. Cir. 2001).

AT&T is wrong on both the facts and the law. In the *Report to Congress*, the Commission did not announce *any* rules -- interpretive or otherwise. To the contrary, recognizing that its distinction between phone-to-phone IP telephony and other forms of IP telephony might not be workable over the long term, the Commission expressly stated that it was not making "any definitive pronouncements" in the *Report to Congress* and said that it would "defer a more definitive resolution of these issues" to a future proceeding with a more fully-developed record.[10] Indeed, far from ruling that AT&T's IP-in-the-middle long distance service is exempt from access charges, the Commission strongly indicated that it would rule otherwise when, in fact, it decided the issue.[11] AT&T's claim that the *Report to Congress* announced a new interpretive rule that would dramatically change the Commission's existing access charge rules is thus a blatant misrepresentation of that *Report*.

Moreover, even if the Commission had wanted to announce such an interpretive rule in the *Report to Congress*, it could not have lawfully done so. Because the APA's notice and comment rulemaking requirements "improve[] the quality of agency rulemaking by exposing regulations to diverse public comment, ensure[] fairness to affected parties, and provide[] a well-developed record that enhances the quality of judicial review,"[12] the interpretive rule exception to these requirements "is to be narrowly construed and only reluctantly countenanced."[13] Thus, a rule may be deemed interpretive and exempt from APA notice and comment requirements only when it provides "clarification of an *existing rule*"[14] or when "it spells out a duty fairly encompassed *within the regulation* that the interpretation purports to construe."[15] By contrast, an agency may not use the interpretive rule exception to "create new law" or "constructively rewrite a regulation or effect a totally different result."[16] It is therefore "well established that an agency may not escape the notice and comment requirements . . . by labeling a major substantive legal addition to a rule [as] a mere interpretation."[17] When a rule "work[s] substantive changes in prior regulations," the APA's notice and comment procedures must be followed.[18]

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[10] *Report to Congress* ¶ 90.

[11] *Report to Congress* ¶¶ 89-91. *See* SBC Memorandum at 4-7.

[12] *Sprint Corp. v. FCC*, 315 F.3d 369, 373 (D.C. Cir. 2003) (internal quotations omitted).

[13] *Sentara-Hampton Gen. Hosp. v. Sullivan*, 980 F.2d 749, 759 (D.C. Cir. 1992) (internal quotations omitted). *See also Orengo Caraballo v. Reich*, 11 F.3d 186, 195 (exceptions to the APA's notice and comment rulemaking requirements are to be construed "narrowly").

[14] *Sprint*, 315 F.3d at 374 (emphasis added).

[15] *Paralyzed Veterans of America v. D.C. Arena L.P.*, 117 F.3d 579, 588 (D.C. Cir. 1997) (emphasis added).

[16] *Sentara-Hampton*, 980 F.2d at 759 (internal quotations omitted).

[17] *Appalachian Power Co. v. EPA*, 208 F.3d 1015, 1024 (D.C. Cir. 2000).

[18] *Sprint*, 315 F.3d at 374. *See also Shalala v. Guernsey Mem. Hosp.*, 514 U.S. 87 (1995) (APA procedures are required if an agency's rule "adopt[s] a new position inconsistent with . . . existing regulations.").

AT&T's characterization of the *Report to Congress* would in fact be a major substantive change in the Commission's access charge rules, not a mere clarification or interpretation. The Commission's longstanding access charge rules -- which have been in place for more than two decades -- require interexchange carriers to pay access charges when they use local exchange switching facilities for the provision of interstate telecommunications services.[19] AT&T has *admitted* to the Commission that its IP-in-the-middle long distance service is a telecommunications service that uses local exchange switching facilities.[20] Under the plain language of section 69.5(b) of the Commission's rules, therefore, AT&T is, and always has been, required to pay access charges on its IP-in-the-middle long distance service. Thus, even if the *Report to Congress* had somehow exempted this service from access charges as AT&T claims (and it did not), the purported "rule" announced in that report clearly would have worked a substantive change in the Commission's access charges rules and therefore would have required the Commission to follow the APA's notice and comment procedures, which the Commission failed to do.[21] AT&T's attempt to couch the *Report to Congress* as an interpretive rule therefore fails, both as a matter of fact and as a matter of law.[22]

(2) AT&T Mischaracterizes the Holding of a Key Supreme Court Decision.

In addressing the question of retroactivity in agency adjudications, the courts distinguish between two types of cases: (1) the application of an existing rule, and (2) the substitution of a new

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[19] 47 C.F.R. § 69.5(b).

[20] Reply Comments of AT&T Corp. at 2, WC Docket No. 02-361 (Jan. 24, 2003) (AT&T Reply Comments); AT&T Petition at 18-19. *See also* SBC Memorandum at 1-4.

[21] *See* SBC Memorandum at 7-9.

[22] AT&T cites *Darrell Andrews Trucking v. Federal Motor Carrier Safety Admin.*, 296 F.3d 1120 (D.C. Cir. 2002), as an example of an interpretive rule that was validly issued without APA notice and comment. But that case has no relevance here. In *Darrell Andrews*, the agency was called upon to interpret its rules governing the records that trucking firms must keep regarding their drivers' activities. Specifically, the agency interpreted the term "supporting documents," which its rules did not define, in such a way as to impose certain record retention duties on trucking firms. Thus, there was no question that the agency was acting to "spell[] out a duty fairly encompassed within the regulation that the interpretation purports to construe." *See Paralyzed Veterans of America*, 117 F.3d at 588. The court in *Darrell Andrews* went on to find that the agency's interpretation of "supporting documents" did not represent a substantial change from any previous interpretation of that term and thus APA notice and comment was not required. Here by contrast, AT&T is asking the Commission to construe the *Report to Congress* not as a mere interpretation of section 69.5(b), but as a substantial modification that would exempt AT&T from paying access charges altogether on its IP-in-the-middle long distance service. Indeed, unlike *Darrell Andrews*, there are no terms in section 69.5(b) for the Commission to "interpret" because AT&T has already admitted that its long distance service is a telecommunications service that uses local exchange switching facilities. Thus, *Darrell Andrews* provides no support for AT&T's position.

rule for an old rule.[23] It is well settled law that when an agency applies its *existing* rules (*i.e.*, Rule 69.5) to a set of facts (*i.e.*, AT&T's IP-in-the-middle long distance service), the "courts start with a presumption in favor of retroactivity."[24] But where an agency substitutes new rules for old rules, courts typically engage in a balancing test that looks at statutory goals or a variety of equitable principles in deciding whether to apply the newly announced rule retroactively.[25]

In a clumsy sleight of hand, AT&T attempts to marry the factual predicate from the first line of cases (applications of existing law) with the legal review required in the second line of cases (balancing test to determine retroactivity). Specifically, citing the Supreme Court's decision in *Chenery*, AT&T states that, even if a Commission decision requiring it to pay access charges qualifies as an application of existing rules (and it does), the Commission must engage in a balancing test to determine whether AT&T should pay retroactively for the past due access charges it has avoided.[26] But this is *not* what *Chenery* held. In *Chenery*, the SEC adopted *new* rules governing the treatment of preferred stock, which broke with prior judicial rulings requiring a different treatment of such stock.[27] In light of this break from precedent, the Court stated that, before applying its *new* rules retroactively, the agency must first engage in a balancing test. Thus, *Chenery* provides absolutely no support whatsoever for AT&T in the instant case, which requires only the application of the Commission's *existing* access charge rules to the facts before it. And, as SBC has demonstrated at length, under these circumstances AT&T is obligated as a matter of law to pay retroactively for the past dues access charges it has illegally avoided.[28]

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AT&T's access avoidance petition has been pending for nearly seventeen months, during which time AT&T has thumbed its nose at the Commission by taking the law into its own hands based on the pretense of an ambiguity in rules that are, in fact, clear on their face. In the meantime, other interexchange carriers that play by the rules and follow the law find themselves at a competitive disadvantage vis-à-vis AT&T, one that will force them, they warn, to follow AT&T's

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[23] *See Verizon*, 269 F.3d at 1109; Williams *Natural Gas Co. v. FERC*, 3 F.3d 1544, 1554 (D.C. Cir. 1993) (citing *Aliceville Hydro Assocs. V. FERC*, 800 F.2 1147, 1152 (D.C. Cir. 1986)); *see also Public Serv. Co. of Colorado v. FERC*, 91 F.3d 1478, 1488 (D.C. Cir. 1996).

[24] *Verizon*, 269 F.3d at 1109 (citing *Health Ins. Ass'n of Am. v. Shalala*, 23 F.3d 412, 424 (D.C. Cir.1994)). *See* SBC Memorandum at 10-11. The presumption of retroactivity may only be rebutted by a showing of "manifest injustice," which requires a party to demonstrate that it detrimentally and reasonably relied on an agency decision. *See* SBC Memorandum at 12. As SBC has explained at length, AT&T has utterly failed to make such a showing. *Id*. at 12-16.

[25] *See Verizon*, 269 F.3d at 1109 (citing *SEC v. Chenery*, 332 U.S. 194, 203 (1947)).

[26] AT&T Memorandum at 14.

[27] *Chenery*, 332 U.S. 194, 203 (1947) (agency decision described as "announcing and applying a new standard of conduct.").

[28] *See* SBC Memorandum at 9-16.

unlawful lead. This situation is untenable and must promptly be addressed by the Commission. Parties on all sides of this issue have called on the Commission to decide the issue expeditiously.[29] SBC now reiterates that call and urges the Commission to immediately deny AT&T's petition and thereby put an end to its unlawful access charge avoidance scheme.

Pursuant to section 1.1206 of the Commission's rules, this letter is being filed electronically with the Commission.

Sincerely,

/s/ *Gary L. Phillips*

Gary L. Phillips

cc(*via electronic mail*):

Chairman Michael K. Powell
Commissioner Kathleen Abernathy
Commissioner Michael Copps
Commissioner Kevin Martin
Commissioner Jonathon Adelstein
Matthew Brill
Daniel Gonzalez
John Rogovin
John Stanley
Paula Silberthau
Jeffrey Carlisle
Tamara Preiss
Michelle Carey
Jennifer McKee
Christopher Libertelli
Jessica Rosenworcel
Scott Bergmann
Jeffrey Dygert
Debra Weiner
William Maher

[29] *See Ex Parte* Letter from David Sieradzki, WilTel, to Marlene Dortch, FCC, WC Docket No. 02-361 (Dec. 3, 2003) ("[C]ompanies need an answer *now* so they can conduct their business on an informed and lawful basis. . . . What the FCC must not do is continue leaving companies to guess -- and litigate -- over what rules apply."); *Ex Parte* Letter from Thomas Jones, Time Warner Telecom, to Marlene Dortch, FCC, WC Docket No. 02-361 (Jan. 9, 2004) (the FCC should make a decision "as soon as possible; the longer the agency waits to make a decision, the more intractable and costly the disputes will become."); WorldCom Comments, WC Docket No. 02-361 at 6 (Dec. 18, 2002) ("The FCC should promptly resolve the policy questions raised by AT&T's petition."); American Internet Service Providers Association, et al Comments, WC Docket No. 02-361 at 3 (Jan. 24, 2003) (the FCC should act "expeditiously" on AT&T's petition); NECA Reply Comments, WC Docket No. 02-361 at 6 (Jan. 24 2003) (the FCC should "dismiss[] the AT&T petition promptly.").